

Amend Revenue and Taxation Code Section 7054 of the Sales and Use Tax Law to authorize the Board to impose a 25% penalty when a taxpayer fails or refuses to timely or adequately furnish any information, documents, or books and records requested in writing by the Board during an examination or audit engagement, unless the failure is due to reasonable cause and is not due to willful neglect. To the extent they are applicable, similar provisions would be incorporated into the Board-administered special taxes and fees programs.

Source: Sales and Use Tax Department

Existing Law

Under existing law, Revenue and Taxation Code Section 7054 authorizes the Board to examine the books, papers, records, and equipment of any person selling tangible personal property and any person liable for the use tax. However, existing law does not provide for a penalty or other monetary disincentive that would apply to taxpayers who fail or refuse to provide the books and records necessary to conduct an examination or an audit engagement (the Government Code authorizes the use of subpoenas to obtain records, however, the process is lengthy and requires the involvement of the Attorney General's office and the Superior Court to compel compliance).

This Proposal

This proposal would authorize the Board to impose a 25% penalty if, during an examination or audit engagement, a taxpayer fails or refuses to furnish any information requested by the date specified in writing by the Board and required under the law. This proposed change in law is similar to Section 19133 of the Revenue and Taxation Code, which authorizes the Franchise Tax Board (FTB) to impose a 25% penalty under similar circumstances.

This proposal is intended to assist in accelerating the sales and use tax revenue stream generated through the Board's audit program by encouraging taxpayers to provide their information, documents, and books and records in a timely manner. In recent years, the Board has noticed a definite trend by taxpayers and/or their representatives to resort to delaying tactics and other strategies in providing requested information, documentation and books and records requested for an examination or audit engagement. This strategy not only delays the entire audit process, it also impacts the Board's audit program and reduces revenue in any given year to the State's General Fund.

The trend or practice of not providing books and records is prevalent statewide. The books and records requested by the Board for an examination or audit engagement are not outside of the norm, but are the normal books of account maintained by an established business entity's normal day-to-day operations and are generally necessary to prepare their financial statements, as well as file their various income and business tax returns.

The Sales and Use Tax Department tracks aged audit assignments on a quarterly basis and has numerous examples each quarter of taxpayers who during an audit

engagement have continually refused to provide or failed to provide the required books and records necessary to conduct an examination or audit engagement in a timely manner. Some of these audits have been known to go on unresolved for up to seven years; some with hundreds of unnecessary audit hours spent in attempting to secure the requested books and records. By reducing the audit time spent on any given audit, the Board will be better able to allocate its audit resources to generate additional revenue and reduce expenses.

According to the FTB, the 25% penalty applicable to its administration of the tax laws (added to the law in 1943) encourages taxpayers' compliance to their information requests when necessary and serves as a disincentive to taxpayers who fail or refuse to provide information, documentation, and the books and records that exist. In a 1997 measure that proposed to repeal this 25% penalty (SB 1166, Hurtt), the FTB noted that if a demand penalty were no longer a consequence of not replying to letters of notice and demand, it is likely that some portion of those replying under current law would not reply under the proposed legislation. Senate Revenue and Taxation Committee staff at that time estimated that the cost of eliminating "this important tax collection tool" could easily be in the \$1 billion range.

It is also proposed that these same provisions be added to the various special taxes and fees programs.

Section 7054 of the Revenue and Taxation Code is amended to read:

7054. The board or any person authorized in writing by it may examine the books, papers, records, and equipment of any person selling tangible personal property and any person liable for the use tax and may investigate the character of the business of the person in order to verify the accuracy of any return made, or, if no return is made by the person, to ascertain and determine the amount required to be paid.

If during an examination or audit engagement, any taxpayer fails or refuses to furnish any information requested by the date specified in writing by the board and required by this part upon notice and demand by the board, then, unless the failure is due to reasonable cause and not willful neglect, the board may add a penalty of 25 percent of the amount of tax determined pursuant to Revenue and Taxation Code section 6481 or any deficiency of tax determined by the board concerning the assessment for which the information was required.